

Economic Policy Reform and Competitiveness Project

QUARTERLY PERFORMANCE REPORT (July - September 2004)

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ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank
AWP-04	Annual work plan for 2004
COP	Chief of Party
CPI	Corruption Perception Index (Transparency International)
DCOP	Deputy Chief of Party
EPRC	Economic Policy Reform and Competitiveness Project
EPSP	Economic Policy Support Project
ERA	Energy Regulatory Authority
FDI	Foreign direct investment
FTA	Free Trade Agreement
FTZ	Free Trade Zone
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GoM	Government of Mongolia
IMF	International Monetary Fund
IR	Intermediate Result
IT	Information technology
LAN	Local area network
LOE	Level of effort
LOP	Life of Project
MoFE	Ministry of Finance and Economy
MOI	Ministry of Infrastructure
MoIT	Ministry of Industry and Trade
MOU	Memorandum of Understanding
M&E	Monitoring and evaluation
P/Ds	Person/days
SO	Strategic objective
SOW	Scope of work
STTA	Short-term technical assistance
TA	Technical assistance
TAF	The Asia Foundation
TCI	The Competitiveness Initiative
TIFA	Trade and Investment Framework Agreement
TORs	Terms of reference
TSG	The Services Group, Inc.
UNDP	United Nations Development Programme
WB	World Bank
WEF	World Economic Forum
WTO	World Trade Organization

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EXECUTIVE SUMMARY: EPRC PROJECT QUARTERLY PERFORMANCE REPORT (JULY - SEPTEMBER 2004)

This Quarterly Performance Report (QPR) for the *Economic Policy Reform and Competitiveness Project* (EPRC) activity covers the period from 1 July through 30 September 2004.

The EPRC contract is a core activity of USAID/Mongolia to support the Mission's Strategic Objective 1, *Accelerate and broaden sustainable, private sector-led economic growth* and its Intermediate Results: Improved enabling environment for private sector growth (IR 1.1) and More competitive industries and sectors (IR 1.2). EPRC will contribute to two broad, interrelated project goals:

1. Accelerate and deepen the policy reform process in Mongolia
2. Promote increased competitiveness in the Mongolian economy.

The relationship between the Mission's strategic framework and the EPRC activity is summarized in the diagram below:

Expected project results include the following:

1. Priority policy issues identified and resolved
2. Improved national dialogue
3. Priority clusters strengthened.

To achieve these results and meet the contract requirements specified by the categories of Contractor's tasks summarized in the adjacent text box, the IP organizes activities in four broad areas:

- A. Economic, trade, and financial policy support
- B. Energy sector reform support
- C. Business and sector/cluster development
- D. Cross-cutting activities: National dialogue and project management

Policy analysis, formulation, and implementation support activities to achieve Project Result 1, *Priority policy issues identified and resolved*, are subsumed under component A of the project. Energy sector reform activities are included under project component B and are also responsive to the achievement of Project Result 1.

Project component C, Business and sector/cluster development, include activities proposed to achieve Project Result 3, *Priority clusters strengthened*.

Project component D responds to the achievement of Project Result 2, *Improved national dialogue*, as well as cross-cutting activities of coordination with other USAID and donors' programs, management of the internship program, and project monitoring and reporting tasks.

Section I of the QPR summarizes significant accomplishments of the quarter:

- Elaboration and intensive discussions with government of a tax reform proposal to promote job creation, formalization of employment and competitiveness
- Organization of a National Cashmere Conference, in partnership with GTZ, to address industry issues
- Analysis of the potential impact of the end of the Multi Fiber Agreement and the quota system on textiles and apparel exports of Mongolia

- Formal constitution of a new leather association, ECO-ARIS, supported by the project to promote Mongolian leather products manufactured in environmentally friendly ways
- Release of a mini CD, *Essential Business Laws of Mongolia*, in partnership with the National Legal Center
- Release of a project-supported *Regulatory Cost Accounting* mini CD by the *Energy Regulatory Authority* containing a manual and training materials for energy companies
- Initiation of a feasibility analysis for a local private venture capital fund conducted jointly with the Mongolian Open Society Forum.

Section I also provides a summary of other activities implemented during the quarter.

Section II of this report presents results of work plan implementation for the quarter.

Section III describes project management and administration activities, current personnel, deployment of short-term expatriate technical assistance, problems encountered and remedial actions, and project and contract management actions for the next quarter.

Annexes A, B, and C contain, respectively, an updated project description sheet, current long-term project staff and details of short-term expatriate technical assignments, and a budget status report.

SECTION I: SIGNIFICANT ACCOMPLISHMENTS

A. Introduction

Pursuant to contract provision F2. (c), this Quarterly Performance Report (QPR) for the *Economic Policy Reform and Competitiveness Project* (EPRC) covers the period from 1 July through 30 September 2004.

Section I of the report describes significant project accomplishments, Section II summarizes work plan implementation, and Section III covers project management and administration. Annexes A, B, and C contain, respectively, an updated project description sheet, current long-term project staff and expatriate short-term assignments, and a budget status report.

B. Significant accomplishments

Project activities resumed an active pace after a relative lull due to the national elections. Contractor's efforts focused on resuming activities put on hold early in the quarter and focused on implementation of the Annual Work Plan for 2004 (AWP-04). By September, the rhythm of project activities was intense, especially in the area of economic policy support. The elaboration of a competitiveness-based tax reform program and intense discussions with the new government, in particular, took center stage.

A close and supportive association with the Mission facilitated the successful accomplishment of projected tasks as planned and no major problems were encountered.

Significant accomplishments of the quarter included the following:

- Elaboration and intensive discussions with government of a tax reform proposal to promote job creation, formalization of employment and competitiveness
- Organization of a National Cashmere Conference, in partnership with GTZ, to address industry issues
- Analysis of the potential impact of the end of the Multi Fiber Agreement and the quota system on textiles and apparel exports of Mongolia
- Formal constitution of a new leather association, ECO-ARIS, supported by the project to promote Mongolian leather products manufactured in environmentally friendly ways
- Release of a mini CD, *Essential Business Laws of Mongolia*, in partnership with the National Legal Center
- Release of a project-supported *Regulatory Cost Accounting* mini CD by the *Energy Regulatory Authority* containing a manual and training materials for energy companies
- Initiation of a feasibility analysis for a local private venture capital fund conducted jointly with the Mongolian Open Society Forum.

The remainder of this section provides a summary of these accomplishments, including other activities implemented during the quarter.

B1. Elaboration and intensive discussions with government of a tax reform proposal to promote job creation, formalization of employment and competitiveness

During September the project focused on four areas of support of the GoM's policy reform agenda, concentrating on measures that could be implemented within 100 days:

1. A package of tax reform measures to address country competitiveness issues
2. Draft of a concession law to provide a suitable legal and regulatory framework to attract private sector financing for infrastructure projects to improve the coverage and quality of service delivery, especially in the energy sector
3. Improving transparency and public participation in the law-making process through retooling of the *Open Government* Web site so that the public has timely notice of proposed new laws and amendments
4. Fulfillment of political campaign promises in a fiscally responsible way.

For the concession law, the project prepared in September two background policy briefs: "Public debt, the energy sector and private investment" and "Energy sector privatization plan."

During the same month, the project released two additional policy briefs dealing with transparency in the law-making process and the fulfillment of campaign promises in a fiscally responsible way. The rationale for the initial tax reform package is summarized below.

A "competitiveness-based" initial tax reform package

The *Mongolia: Vision 2020* draft economic development strategy prepared during the first quarter of 2004 at the request of the Prime Minister's Office identified tax policy as one of the constraints to be addressed to facilitate private sector led economic growth and improve country competitiveness. The latter is of particular concern in light of Mongolia's export performance over the last decade.

The value in current prices of Mongolia's exports, other than those from mining and textiles, has declined over the last decade. And the impact of the end of the Multi Fiber Agreement at the end of this year is likely to diminish the value of these exports even further as companies currently using the protection of this scheme move out of Mongolia. Thus, other than the export of raw metals and minerals, the Mongolian economy is failing to turn its limited comparative advantages into competitive edges to benefit from participation in the world economy. Fundamentally, the country is not selling abroad.

Realizing the vision of a competitive participation of Mongolia in the world economy requires, *inter alia*, a tax system that is aligned with government policies promoting private sector led economic growth. Mongolia's tax system at present is not aligned with such policies. In fact, many of its provisions provide a perverse system of incentives that place unnecessary burdens on businesses, support a shadow economy, act against job creation, and discriminate against domestic businesses. Current tax policies and their administration send "wrong signals" to businesses.

Constructed piece meal over the last fifteen years as Mongolia began its transition to a market-oriented economy, the tax system now requires an overhaul. Given the magnitude of the task and the urgency of some tax reform measures, a practical, staged approach is required:

1. A “competitiveness-based” tax reform package needs to address the most glaring anti-competitiveness provisions of the Mongolian economy. This is the package of reforms that the project has been focusing on and discussing with the GoM.
2. A general review and overhaul of provisions, regulations, concepts and definitions scattered in different laws and decrees that are often contradictory, unclear, incomplete or contrary to international best practices. This work will be initiated with the assistance of the International Monetary Fund (IMF) in October.
3. An overall review of budget expenditures and their reorientation towards economic growth and poverty reduction in line with Mongolia’s commitments. It is our understanding that the World Bank will provide support to the GoM in this regard.
4. A program to improve tax administration (internal systems and procedures, operational regulations, auditing capabilities, large tax payer office, etc.). This is likely to require a two-year well-designed and executed program. Funding for this program at the General Department of Taxation (DGT) will need to be secured, perhaps by reactivating negotiations on a loan agreement with EBRD.

It should be noted that these four separate programs or stages need to take into consideration fiscal balance requirements and size of the state budget. The size of the fiscal deficit needs to be reduced to achieve fiscal balance and consideration must be given to the size of the budget relative to Mongolia’s Gross Domestic Product (GDP) or size of the economy.

The proposed “competitiveness-based” tax reform package for which the project is providing support to the GoM has six inter-related objectives:

1. Reduction of the cost structure of firms (taxes on labor) to improve their competitiveness
2. Unification of the personal income tax to reduce the tax burden on lower-income wage earners and on labor costs associated with higher income workers to diminish the size of the shadow economy
3. Reduction of the burden placed on domestic businesses by high corporate tax rates and administrative/legislative distortions
4. Supporting the development of domestic businesses by shifting the tax burden to change relative prices in the economy in favor of domestic producers vis-à-vis foreign producers
5. Shifting the tax burden from investment/production towards consumption/ownership
6. Preservation of the overall integrity of projected fiscal revenues in line with fiscal prudence and commitments to international finance institutions.

During the next months the project, in collaboration with multilateral agencies and bilateral organizations, intends to continue to provide support on the revision of tax policies and other “100-day measures”, as requested by the GoM. The project will continue to work closely with the Office of the Prime Minister, Parliament and Members of Parliament, Ministry of Finance and Economy (MoFE), the General Department of Taxation (DGT), the business community, relevant organizations, and civil society. A working public consensus coupled with the strong political will shown so far by the coalition government will be required to enact these much needed reforms to improve Mongolia’s competitiveness.

B2. Organization of a *National Cashmere Conference*, in partnership with GTZ, to address industry issues

A National Cashmere Conference, jointly sponsored by the project and Deutsche Gesellschaft fuer Technische Zusammenarbeit (GTZ), was held at the Chinggis Khan Hotel, Ulaanbaatar, on July 6th 2004. The conference called on the industry and government to work together to improve the competitiveness of Mongolian cashmere in global markets.

The conference, *Cashmere: a partnership for the future* brought together industry leaders, government officials and researchers to discuss key issues faced by the industry in the light of increased competition from China, and the imminent withdrawal of the Multi Fiber Agreement in 2005. It covered a range of topics including herd improvement, procurement, and the need to add more value to exported cashmere.

The conference was prompted by the publication of a report by Dietmar Stiel, of Seco Sector Consulting, and commissioned by GTZ, that compared the developments in the Chinese cashmere industry with the current situation in Mongolia. The report highlighted how investment in new technologies and know-how by the Chinese had led to improved production efficiencies, better quality, the ability to produce a wider range of products, and improved reliability. Lack of investment in the Mongolian industry was allowing it to slip further behind the Chinese. Mr Stiel emphasized the need for more foreign direct investment and know-how in the industry and called on the government to provide the conditions and incentives to attract such investment. Mr Stiel defined Mongolia's strength as its strong raw material base and relatively low production costs and suggested that opportunities could arise as the demand for pure cashmere products increased. He told the conference that the industry's future lay in producing 100% Mongolian cashmere products to niche, premium price markets.

The conference included presentations by EPRC staff. Christopher Broxholme delivered a paper on the end of the textile quota systems brought about by the end of the Multi Fiber Agreement in 2005. Bruce Harris presented a framework for industry cooperation in light of Chinese competition in the cashmere market.

By far the most contentious issue to be debated was the question of whether the Mongolian industry should be protected by a ban on the export of raw cashmere or the imposition of prohibitive export tariffs. Manufacturers and processors argued that the illegal export of raw cashmere, estimated at up to 60% of total production, was distorting the market, making it impossible for them to compete. They contended that inward investment was at its highest when the Mongolian government banned the export of raw cashmere in the mid-nineties and supplies were secure. These arguments were countered by herders' representatives, believing that rural incomes would decline dramatically if such prohibitions were introduced, and claiming that



illegal exports would in fact increase due to the inability of the authorities to police the borders. The economists present at the conference supported this view and pressed for an in depth examination of the long term consequences of protectionist policies.

Less controversial was the call by delegates to combine efforts to promote Mongolian cashmere on international markets. The first step had been the introduction of the Fibermark to distinguish Mongolian cashmere from its competition. The Fibermark Society, which was founded by all the leading Mongolian manufacturers, was gaining support and international recognition, providing a basis for co-operation within the industry.

Despite disagreements, all delegates recognized the need to work together and backed a call for the industry to set up a national working group to develop a country strategy for the industry. The call was welcomed by the State Secretary at the Ministry of Industry and Trade who told the conference that the government would welcome any private sector led initiative which could help frame future policy for the industry. It was agreed that the conference organizers would draw up an agenda for action as the first step in forming the working group.

The project plans to support the working group through the conduct of a value chain analysis in the fall as a framework for developing concrete policy proposals for government and private sector action to improve the competitiveness of the cashmere cluster.

B3. Analysis of the potential impact of the end of the Multi Fiber Agreement and the quota system on textiles and apparel exports of Mongolia

Since the early 1970's the United States (US), the European Union (EU), Canada and Norway have maintained strict limits (quotas) on the amounts of textile and apparel products entering their markets. These limits were maintained especially against low-cost producers' products and were in addition to usual taxes levied on imports such as customs duties or VAT. The Multi-Fiber Agreement of 1974 (MFA) permitted such quotas to be maintained, notwithstanding the general prohibition of the General Agreement on Tariffs and Trade (GATT) on import and export restrictions.

The US, EU, Canada, and Norway concluded a large number of bilateral agreements with developing countries, within the framework of the MFA, setting strict limits on imports of textiles and clothing. However, in order to secure agreement to the Uruguay Round of trade agreements (1994) and the establishment of the World Trade Organization (WTO) it was necessary for these countries to concede that GATT disciplines should be extended to include textiles and clothing. The system of quotas for fibers generally was agreed to be phased out over a ten year period under the Agreement on Textiles and Clothing (ATC).

A draft Briefing Paper prepared by the project, *Potential Impact of the end of the Multi Fiber Agreement on Mongolia's textile industry*, examines the implications for the apparel and textile industry in the country and outlines proposals for mitigating such impact.

The MFA quotas have been subject to a four-stage integration into quota-free trade. Integration has taken place already in the periods 1995-97 and 1998-2001 and is taking place for the period 2002-2004. The largest integration of quotas will occur on 1 January 2005 when about half of the remaining products will have quotas removed. This last half is made up of the most sensitive

products for the US, EU, Canada, and Norway—those which these countries make themselves domestically.

There is likely to be an increase in competition in the US market following the removal of quotas, savings in production costs for producers in former quota countries, and the end of the need for purchasers in the US to take their supplies from multiple suppliers.

Producers based in countries which are currently subject to quotas will be able to sell unrestricted amounts of textiles and apparel in the rich markets of the US, EU, Canada and Norway. They will benefit from economies of scale, with the need for artificially reduced product runs eliminated.

Mongolia has attracted investment in textile and apparel industries, mostly from China and Hong Kong. An advantage of manufacturing products in Mongolia—quota-free access to the US—will come to an end. As shown in Exhibit I-1, forty-eight countries will be eligible to gain quota-free access to the U.S. markets for their apparel products.

Producers will no longer need to relocate manufacturing facilities to countries which have not been subject to quota for a particular product or send material to those countries to be made up into garments in order to take advantage of their quota-free status.

Mongolia's exports to the US are mostly made-up of cotton apparel products. The cotton is imported and, with some exceptions, attracts import duties. Assuming no capacity constraints in the producers' home countries, there would be no need to move material to Mongolia for such value to be added and duties paid. Mongolia has no domestic cotton production.

Purchasers of textile and apparel products in the markets of the US, EU, Canada, and Norway will be able to source their products from fewer supplier countries since the quota-free advantage will have been eliminated. They may choose countries with a wide range of value-added products. To the extent that Mongolia competes in products with countries able to supply large quantities with attendant economies of scale, it is likely to lose market share. Regrettably Mongolia offers very restricted product ranges at the current time.

Exhibit I-2 shows Mongolian apparel products likely to face increased competition in the U.S. markets as a result of the end of the quota system. Using 2003 figures, the total value at risk of

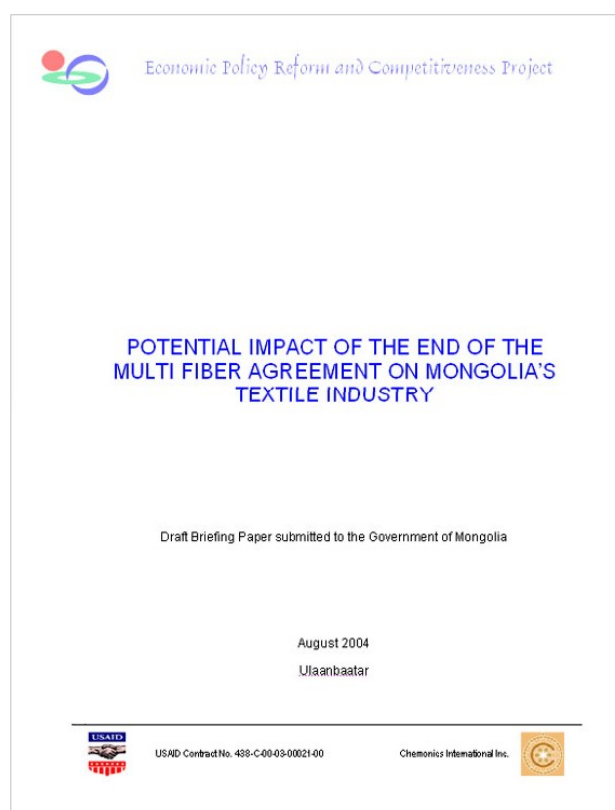


Exhibit I-1: Countries which will gain quota-free access to the U.S. on 1 January 2005

Bahrain	India	Pakistan
Bangladesh	Indonesia	Panama
Brazil	Jamaica	Philippines
Bulgaria	Japan	Poland
China	Korea	Qatar
Colombia	Kuwait	Romania
Costa Rica	Laos	Singapore
Czech Rep.	Lesotho	Slovakia
Dominican Rep.	Macau	Sri Lanka
Egypt	Macedonia	Taiwan
El Salvador	Malaysia	Thailand
Fiji	Mauritius	Turkey
Guatemala	Mexico	United Arab Emirates
Haiti	Myanmar	Uruguay
Hong Kong	Nepal	Ukraine
Hungary	Oman	Vietnam?

Mongolian textile and apparel exports is slightly over US\$ 183 million. Thus, the removal of quotas on 1 January 2005 is likely to prove costly for Mongolia in terms of textile and apparel exports and jobs which depend on these.

As a member of the World Trade Organization (WTO), Mongolia's policy options are tied to the Agreement on Textiles and Clothing (ATC) and its unrelenting timetable for quota removal. This timetable seems unlikely to change.

What to do? Rather than expending resources on participation in debates, which Mongolia will not influence, government and industry should confer around the following subjects:

1. Analysis of apparel producers' cost structures, target markets, identification, and implementation of measures to improve their competitiveness

Although it may be too little too late, industry and government must confer and identify non-distortionary and WTO-compliant measures that at least in the short run will mitigate the impact of the end of the quota system for apparel products.

EPRC can support these discussions by assisting industry and government in analyzing comparative cost structures and helping with the identification of such policies. An apparel industry specialist supported by the project will begin such work in late September.

2. Diversification away from quota-constrained products and towards products which still offer tariff protection in the U.S.

In the medium term but starting now, the local apparel industry should explore diversification into products that are not quota constrained. The draft Briefing Paper prepared by EPRC provides an initial analysis of such possibilities.

3. Apparel export diversification away from reliance on the U.S. markets

98% of Mongolia's textiles and apparel is exported to the US market. This makes Mongolia highly susceptible to policy initiatives which may be taken in the US aimed at China, but broadly written to circumvent the non-discriminatory provisions of the General Agreement on Tariffs and Trade (GATT). Mongolia should closely follow US government

Exhibit I-2: Mongolia's exports to the U.S. which will face increased competition from 1 January 2005

HTSUS Product	Description	Value of exports to the U.S. (USD)
61102020	Sweaters, pullovers and similar articles, knitted or crocheted, of cotton, nesoi	64,621,015
62046240	Women's or girl's trousers, breeches and shorts, not knitted or crocheted, of cotton	38,061,677
61101210	Sweaters, pullovers, sweatshirts, waistcoats and similar articles, knitted or crocheted, of cashmere.	9,847,032
61046220	Women's or girls' trousers, breeches and shorts, knitted or crocheted, of cotton	8,305,980
62034240	Men's or boys' trousers and shorts of cotton	7,170,095
62052020	Men's or boys' shirts, not knitted or crocheted, of cotton	5,798,687
61051000	Men's or boys' shirts, knitted or crocheted, of cotton	4,593,659
63023190	Bed linen, not knitted or crocheted, not printed, of cotton	3,983,883
62019220	Men's or boys' anoraks, windbreakers and similar articles, nesoi, not knitted or crocheted	3,581,132
62053020	Men's or boys' shirts, not knitted or crocheted, of man-made fibers, nesoi.	2,605,335

actions to ensure it is not ensnared in Sino-US trade disputes.

The European Union (EU) is an additional market which offers some trade preferences for textiles and apparel. The EU grants tariff reduction of 20% off current Most Favored Nation (MFN) rates for Mongolian textiles and apparel, including Mongolia's major exports. Mongolia must convince the EU that its labor standards meet international minima and benefit from significant additional tariff reductions.

The project supported the MoIT in its application to the EU to examine Mongolia's compliance with international labor standards and the application received favorable response from the EU Trade Commissioner this spring. As no dates have been set for the survey of labor practices and the process of certification may take 12 to 24 months, access to the potentially significant tariff reductions in the EU markets cannot be relied upon in the short run.

4. Industry consolidation and product range

After 2005 major purchasers of textile and apparel products are likely to favor suppliers of wide ranges of products. Mongolian producers should try to maximize economies of scale by co-operation and co-ordination within the industry. In addition, the identity of Mongolian products, as distinct from Chinese, should be supported.

As the end of the apparel quota system will likely cause some foreign investors to pull out of Mongolia, remaining producers will have to diversify and improve their product range, maintain competitive cost structures, and achieve economies of scale to remain competitive.

The draft Briefing Paper also examines additional medium-term trade policy actions in detail. Given the pressing nature of the subject, EPRC proposes a focus on immediate measures that need to be considered. To that effect, an apparel industry specialist will assist the project, industry, and government beginning in late September to:

- Conduct a rapid assessment of apparel companies' capacities, product ranges, pricing structures, etc., to gauge competitive potential
- Assess apparel companies' management intentions regarding their Mongolian plants and obtain suggestions for measures that the GoM may take that would weigh heavily in their decision to stay in or leave the country in the aftermath of the end of the quota system
- Provide recommendations to selected firms to improve their competitiveness
- Prepare projections of likely job losses and the timing of the losses under different scenarios
- Identify a comprehensive list of interim measures and non-distortionary incentives for adoption by the GoM
- Assist industry and government in the discussion and negotiations of these measures.

How much success these short-term measures will have remains an open question. There is now little time left given the inexorability of the end of the quota system whose end date has been known well in advance by all parties.

As the fate of some 40,000 workers employed in some 66 known companies operating in Mongolia and exports worth over US\$ 183 million are at stake, any effort to mitigate impact, no matter how late is worth trying.

B4. Formal constitution of a new leather association, ECO-ARIS, supported by the project to promote Mongolian leather products manufactured in environmentally friendly ways

A new association of Mongolian leather producers has been formed to promote leather products on domestic and international markets. The association announced its formation, its aims and objectives at a press conference at the Brauhaus restaurant on the 7th July 2004.

The association, *ECO-ARIS*, has been founded by eleven independent businesses to develop a competitive advantage for Mongolian leather by encouraging cooperation among members, sharing equipment and technology, combining resources to market Mongolian leather, and introducing joint purchasing initiatives for raw materials.

As the name implies the members are committed to producing leather in an environmentally friendly way by ensuring that only safe chemicals are used in the process, reducing pollution in their waste water emissions, and maintaining a healthy and safe working environment.



The group, which is being advised by the project, understands that to compete in the world leather markets they need to work together to improve productivity, quality, and marketing. Most hides are exported to China as ‘wet-blue’, hardly processed at all, but the association members intend to add more value to the leather in Mongolia, to attract premium prices and create more employment. Each of the member companies has different strengths and as a group they hope to turn those strengths into a competitive advantage. The association will act as real business association, providing practical business help to its members. The association will also represent the views of its members with regard to shaping industry policy, but the association will be “non-political”.

Bruce Harris, EPRC’s Senior Business Development Advisor, explained the involvement of USAID in these terms: *“Experience from around the world shows us that industrial performance and competitiveness can be dramatically improved if businesses work together in groups or clusters. This new association is a perfect example of what is known as ‘cluster development’, and the type of project that USAID and EPRC are very happy to support”*.

The association was formed in April and finished its formal registration process in June. Its eleven founder members are: BSB Co., Ltd., Darkhan Nekhii Shareholding Company, Darkhan Minj Co., Ltd., Buyantugs Co., Ltd., Chrome Trade Co., Ltd., Yuroolt International Co., Ltd., Buural Gol Co., Ltd., MLTJ Co., Ltd., Devjikh Trade Co., Ltd., Ad Chem. Co., Ltd., and B.Nergui. The Association hopes to attract new members when other companies see the benefits of joining, but intends to enforce high entry standards to protect the reputation of the association.

B5. Release of a mini CD, Essential Business Laws of Mongolia, in partnership with the National Legal Center

On 14 September, at the 7th Annual Investors Conference, the *National Legal Center* (NLC) and the project presented the first release of Mongolian and English versions of *Essential Business Laws of Mongolia*.

The initial release, in mini CD format, contained twenty laws updated with all current amendments in both languages as well as an index of bilateral and multilateral international agreements of which Mongolia is a signatory. Initiated in May in partnership with the project and its subcontractor, The Asia Foundation, the release will provide easy access to texts of laws and all amendments for Mongolian businesses, foreign investors, and the general public. The product is a first step to improve public access to laws and their amendments and intended to remedy a situation where access to the texts of laws is scattered and the texts have not been updated to reflect all current amendments. For example, previously available postings of Mongolia's corporate income tax law (Law on Taxation of Economic Entities) contained twenty amendments when in fact there have been twenty nine.



These updated business laws, in Mongolian and English, will also be posted in the NLC Web site as they become available. Web sites of government ministries and agencies will provide links pointing to the NLC Web site as a consolidated repository of updated laws, as provided in NLC's legal charter.

Potential foreign investors, as well as other interested parties, will be able to access relevant business Mongolian laws in English from anywhere in the world through the Internet.

A second release, expected to be completed during the first quarter of 2005, will contain updated versions in Mongolian and English of twenty additional business laws. These texts will also be posted in the NLC Web site for public access.



B6. Release of a project-supported Regulatory Cost Accounting mini CD by the Energy Regulatory Authority containing a manual and training materials for energy companies

In preparation for the workshops that will begin on October 6 for the Central Energy System (CES) generating companies, the project completed and released a manual on regulatory cost accounting at the end of September. The manual and related training materials were released in a mini CD as well as printed copies.

The workshops will focus on procedures for conversion and restatement of accounts according to International Accounting and Financial Reporting Standards (IAFRS). Target participants for the workshops include CES generating company accountants, Ministry of Finance and Economy (MoFE), State Property Committee (SPC) and ERA staffs.

The companies are mandated by the ERA to start using the system with the beginning of their new fiscal year on 1 January 2005. Between now and November, the new cost accounting methods will be implemented at the energy generation level and the project will provide selective on-site guidance on cost accounting and conversion of accounts, as needed, to individual companies.



Distribution, transmission and other entities are tentatively scheduled for implementation assistance during the first half of 2005.

Approval of the Energy Sector Chart of Accounts

With the assistance of our Mongolian accounting subcontractor and the project's energy accounting staff, the ERA made the official submittal to the Ministry of Finance and Economy for approval of the new chart of accounts for energy companies. When MoFE grants its approval—expected in October—use of the chart of accounts by energy companies will become mandatory.

B7. Initiation of a feasibility analysis for a local private venture capital fund conducted jointly with the Mongolian Open Society Forum

Partnering with the *Open Society Forum* (OSF), the project initiated in September the feasibility analysis for the establishment of a local private equity fund. Initial findings in the Mongolian market were favorable with regard to four broad issues that the feasibility analysis was designed to address:

1. *Deal flow*: Preliminary findings indicate that there are enough companies and ventures with high-growth potential that could yield competitive returns to the fund and benefit from equity and quasi equity investments; detailed profiles of the companies, their financials, and growth opportunities will next be required to solidify prospective commitments from investors and prepare a prospectus.
2. *Local private investors' commitments*: Preliminary local private investors' commitments have been obtained subject to conditions that include, *inter alia*, anchor investments by multilateral financing institutions and professional, international management of the venture capital company; these initial private sector Mongolian commitments, one of the "acid tests" of the venture fund, will be contingent upon further documentation of a suitable pipeline of potential transactions—deal flow—as detailed under item 1, above.
3. *Commitments from international finance institutions (IFIs) and bilaterals*: Preliminary agreement to pursue approvals to participate as anchor investors in the prospective local private venture capital fund was obtained from one IFI and the participation of another was in process; close cooperation among all potential anchor investment partners will be required in parallel with activities in documenting deal flow and pursuing private investors' commitments—items 1 and 2, above.
4. *Grant-funded assistance to provide commercial returns to investors*: Given the likely small size of the private venture capital fund (perhaps \$8 to \$12m) and the incipient state of Mongolian companies, normal management fees will be unable to cover the venture capital fund company expenses; initial commitments to fund this component will need to be elicited from partner institutions concurrent with activities under items 1 through 3, above.

A formal presentation of preliminary findings and forward strategy is scheduled for mid October.

B8. Other activities implemented in the quarter

B8.1 Other activities in economic and trade policy support

Shadow economy survey in partnership with the Mongolian Foundation for Open Society. The project continued to work closely during the quarter with the Mongolian Foundation for Open Society (MFOS) and the National Statistical Office (NSO) on a survey of the shadow economy. Results from a pretest of the household questionnaire were tabulated and examined and the data collection instrument was revised. The project is currently negotiating a subcontract agreement with MFOS to assist in the data collection and processing effort and obtain all data sets for specialized analyses of segments of the shadow economy of special interest to the project.

Overview of the Mongolian Tax System. Short-term taxation expert, Mr. Rup Khadka, worked during the quarter on an overall assessment of taxation, with a special emphasis on the impact of these policies on private sector led economic growth, job creation, and country competitiveness. Taxation policies were identified as a priority area of concern in the national economic development strategy draft paper prepared last spring at the request of the Prime Minister's Office. The following tasks were included in the assessment:

- Analyze the current tax regime (based on available legislation/regulations)
- Collect information, from both businesses/NGOs and governmental agencies on the actual implementation of the laws

- Identify relevant problems and document them (legal base, nature of the problem, supporting evidence, etc.)
- Verify the accuracy of problem description and its legal base
- Document/explain the effects of each problem on the economy
- Formulate recommendations on how to fix the problems
- Formulate criteria for policy priorities and based on these criteria formulate actionable plans for each.

The overall tax policy assessment was used to elaborate concrete proposals for changes in tax legislation and regulations that the project submitted to the GoM for consideration of inclusion in its economic policy reform agenda. A discussion draft of the report on the Mongolian tax system was completed during the quarter and is scheduled for release early in the next quarter.

Assistance with the preparation of a 100-day economic policy reform agenda for the new government. The first few months after effective start-up of a new administration are critical in setting the course and achieving reforms. A short window of opportunity exists for developing consensus around a core set of key “first stage” reforms, preparing “actionable” technical proposals, initiating their execution and getting commitments for second and third stage reforms which require more complex analysis and wider discussion.

The project worked during the quarter on a tiered set of actionable economic policy reform proposals and held initial discussions with GoM counterparts. Brief concept papers were circulated in early September for discussion with GoM key decision makers with the objective of getting a “buy in” and decisions to develop specific technically supported actionable proposals for discussion and adoption at Cabinet and Ikh Hural levels.

Impact of ATC and MFA. The project completed a draft technical paper on Impact scenarios of the Agreement on Textiles and Clothing (ATC) and Multi Fiber Agreement (MFA) on Mongolian textiles quota-free access to U.S. markets and sketched out potential scenarios and industry options.

Assistance to the Ministry of Industry and Trade (MoIT) in preparation for TIFA. At the request of MoIT, the project prepared terms of reference (TORs) for an international trade specialist to assist with preparations for TIFA meetings. By the end of the quarter, TORs were being discussed and cleared with USAID for submission to MoIT and engagement of a specialist.

B8.2 Other activities in sector/cluster and firm competitiveness

Tourist facilities fact-finding tour. The project organized and completed a 13-day fact finding tour of Hovsgol, Arkhangai, Ovorhangai, and Bulgan—a 3,000 km. itinerary. The group visited 38 ger camps, took 2,900 photos and interviewed 38 ger camp managers/directors. The visited facilities constitute approximately thirty-five percent of registered establishments of this type. The group performing the assessment included representatives from the Mongolian Tourist Association, and the Mongolian Tourism Board.

Issues identified in the assessment included extreme variations in levels of service and amenities available among the establishments, low levels of cooperation among camps, tour operators, and

service providers, low levels of training of a largely transient labor force in the industry, a need to overhaul and improve training delivery in the industry.

Meeting of the National Cashmere Working Group. EPRC facilitated a meeting of key members of the cashmere industry to begin the process of forming the National Cashmere Working Group, as proposed at the EPRC/GTZ Cashmere Conference held in July. The group met twice during the quarter and has the backing of a caucus of eleven newly elected MPs (The “Cashmere Caucus”), D.Gankhhuyaj, R.Badamdandin, B.Batbayar, B.Jargalsaikhan, Ch.Ulaan, S.Batbold, Ts Bayarsaikhan, Tsengel, Zorigt, A.Bakei, Tuya. The project will prepare TORs for a short-term assignment to conduct a value-chain-based analysis of existing policies affecting cashmere, prepare actionable proposals for changes in these policies and regulations and act as an initial advisor to the working group.

European Distribution Network. The project continued to act as conduit between Germany and Mongolia for the cashmere European distribution network, specifically assisting with the documentation for the GmbH (German limited company). The principal traveled again to Ulaanbaatar in September to allocate share certificates and finalize legal registration requirements. Preparation samples also began for the Berlin-based center for distribution of Mongolian cashmere in the European markets. These samples are scheduled for shipment to Berlin early in the next quarter.

Support of FiberMark Society. Banners and brochures of the society were distributed to all Mongolian cashmere outlets. The project also supported the publication of the first issue of the Society’s weekly, *Market Report*. Subcontract negotiations to complete the registration process of FiberMark’s trademarks in selected international markets continued, with a special emphasis on registrations in the European Union.

Measures to mitigate impact on Mongolia the end of Multi Fiber Agreement. The project prepared terms of reference and engaged an international textile specialist to examine the cost structure of Mongolia-based apparel firms and propose measures to mitigate impact. The specialist attended the international meeting in Bangkok organized by The Asia Foundation, participated in panel discussions, met the Mongolian delegation and EPRC’s Senior Business Development Advisor, Bruce Harris. The international specialist is expected to begin his assignment in Mongolia during the third week of October.

B8.3 Other activities in energy sector policy support

Electric Distribution/Supply Licenses: The ERA requested project assistance with the preparation of a number of sector company licenses which need to be issued in September and October 2004. We drafted a set of standard provisions for all licenses. New items included the Obligation to Serve, *Force Majeure* and streamlining of the periodic reporting requirements. Specifically, we assisted with the drafting of:

- A Distribution License for the Darhan-Selenge Electric Distribution Company
- A Supply License for the Darhan-Selenge Electric Distribution Company
- A Distribution License for the Bagnuur Electric Distribution Company
- A Supply License for the Bagnuur Electric Distribution Company.

Construction Licenses: This subject became acute when we learned that a private Mongolian company intends to request a license to construct a pump storage hydro electric project. To date, no construction license has been issued for a major project sponsored by a private developer. In preparation of our drafting of a procedure to apply for a License to Construct an Energy Generating Facility, we met with the developer, suggested project development steps and milestones to the company, and proposed a pooling of interests with another company contemplating a similar project. We also initiate a review of current construction license forms issued by the ERA in the past.

Market and Tariff Structures: These are two World Bank-initiated projects which have received our support. The WB consultant visited Mongolia and is now preparing his recommendations. EPRC expects to be asked by the ERA to assist with the implementation. In doing our own research, we realized and advised the World Bank that there are technical constraints to the implementation of a competitive market structure and decided to prepare TORs for a technical consultant to review those shortcomings and advise all parties involved on what the actual needs are.

Preparation completed for workshops on account conversion and restatement of accounts in IAFRS format. All training materials for the workshops starting October 6 for the Central Energy System (CES) generating companies were completed. The workshops will run six days spread over two weeks. This work will continue with visits to the individual generating companies, where we will provide them with specific guidance on their cost accounting and conversion problems. The workshops will include CES generating company accountants, Ministry of Finance and Economy (MoFE), State Property Committee (SPC) and ERA staffs. The companies are mandated by the ERA to start using the system with the beginning of their new fiscal year, on 1 January 2005.

ERA Public Hearing Procedures: Because the ERA intended to raise tariffs for heat and electricity in September, they asked the project to assist them with drafting an interim Public Hearing Procedure. The Interim Procedure suggested by the project was approved by the ERA on August 24, 2002. It is subject to review and revision when the project brings a short-term public communications specialist in October to assist ERA on this matter.

Public Communications Procedures: The project finalized TORs and engaged a short-term consultant to assist the ERA in writing a number of procedures, including public hearing, cold weather disconnection, public education, dispute resolution and a consumer protection program. The assignment is scheduled to begin in early October.

Preparation of two EPRC Policy Briefs. The project prepared two energy sector related Policy Briefs:

1. Public Debt, The Energy Sector and Private Investment, discussed the effect financing by public debt on the condition of the sector, and proposed that all future investment originate from private sources to reduce the overall investor country risk and preserve Mongolia's sovereign credit rating.
2. The second Policy Brief puts forth our recommendation for the new government's Energy Sector Privatization Plan and promotes the passage of a Concession Law to accelerate privatization at reduced investor risks. This Brief is a follow up to our recommendations made in July 2004 to the State Property Committee, where we made specific

recommendations as to procedure and plans for the privatization of certain groups and individual companies. Some of the background was drawn from a short paper we distributed to stakeholders on the most common methods of privatization, ranging from Management Contracts to 100% Asset Sales.

Fourth Bimonthly Energy Donor Round Table: On August 27, the project hosted the fourth bimonthly meeting of the Energy Donor Round Table. The meeting was attended by UNDP, EBRD, GTZ and KfW. Subjects of major discussion were energy conservation, updating the energy law, technical assistance to the National Distribution Center and privatization efforts in Zavkhan Aimag.

Private Sector Interactions

- At the request of USAID Mongolia, we met with Ivanhoe Mines and the Ministry of Infrastructure to facilitate their discussions of how to best supply power to Ivanhoe's Oyu Tolgoi mining project and made suggestions on a strategy.
- We met with a Mongolian company which controls a coal mining exploration license to discuss with them how they could benefit from developing their property, supplying electricity to Tavan Tolgoi and another proposed mining project, develop an electricity export market to China, discussed steam coal and metallurgical coal exports to China, Japan and Korea, and proposed for them to consider a project to convert coal into naphtha for further refinement into diesel and gasoline for Mongolian consumption. We offered to assist them to identify consultants who could help them identify potential project partners with the requisite financial resources.
- As stated above, we met with a company interested in developing a pump storage hydro project and put them in touch with a potential partner for the project.

B8.4 Other activities in public education and national dialogue support

Strengthening public participation and input in the law making process. The project, partnering with the *National Legal Center* and *The Asia Foundation* continued work on a proposal to streamline the process of submissions and discussions of proposed laws. Objectives are to simplify the process and establish a transparent protocol for public comments at each draft stage of proposed legislation. The proposal will suggest changes in GoM Resolution 2000-No 178 on Cabinet Procedural Rules, the Law on Drafting and Submitting Laws & Other Resolutions of the Ikh Hural of 8 November 2001, and Ikh Hural Resolution of 21 June 2001, No. 61 and its Amendment of 13 May 2004 establishing the legal process of law making. The proposal will also include explicit provisions for public posting the different drafts of a proposed law in the *Open Government* Web site, with appropriate periods for public comment and input.

SECTION II: WORK PLAN IMPLEMENTATION

A. Introduction

This section documents project implementation status of the current work plan—AWP-04—as of the end of the quarter. Part B of the section presents the framework of AWP-04 for the four project components: Economic, Trade, and Financial Policy Support, Energy Sector Reform Support, Business and Cluster Development, and Cross-Cutting Project Activities and Management. The framework contains objectives, projected annual results, and projected life-of-project (LOP) results for each component; the first column contains the objectives defined in the strategy, the second column contains the expected results at the end of the first annual work plan and the third column details the status at the end of the project.

Part C of the section contains detailed implementation status by project component.

B. Work plan framework

The work plan framework for Economic, trade, and financial policy support is as follows:

A. ECONOMIC, TRADE, AND FINANCIAL POLICY SUPPORT		
Policy Support Objectives	Projected annual results	LOP Results
A1. Development, maintenance, and implementation of sound macroeconomic policies to promote sustainable and equitable economic growth	Fiscal and macroeconomic impact analysis of foreign debt service projections and policy options developed and presented.	A stable and predictable macroeconomic environment, market-oriented, and promoting sustainable and equitable economic growth.
	Fiscal and macroeconomic impact scenarios of corporate tax reduction developed; policy options formulated and presented.	
A2. Development, maintenance, and implementation of trade and investment policies supportive of a competitive participation of Mongolia in the world economy	Generic tariff and non-tariff barriers to Mongolia's trade expansion in Russian and Chinese markets assessed for bilateral and multilateral negotiations.	Generalized reduction of tariff and non-tariff barriers to trade with trading partners.
	Improved information access available for entrepreneurs on foreign target markets' entry requirements and GSP applicable to Mongolian products.	Mongolia utilizes existing trade mechanisms and/or negotiates better access of specific export products having an identified demand in trading partners' markets.
	Impact scenarios of the <i>Agreement on Textiles and Clothing</i> (ATC) and <i>Multi Fibre Agreement</i> (MFA) on Mongolian textiles quota-free access to U.S. markets and formulation of policy and industry options.	Trade and export strategy leads to negotiation of free-trade agreements (FTAs) with countries providing net advantages to Mongolia in terms of trade.
A3. Reduction of transaction costs for businesses	Assessment of Bank of Mongolia requirements, banking spreads, and formulation of policy instruments and plan of action to induce a reduction of commercial loan interest rates, consistent with a stable, market-oriented macroeconomic environment.	Reduction of cost of loan capital to businesses.
	Field investigation of Russian and Chinese practices applied to the transit of selected Mongolian products and elaboration of GATT-supported procedures for negotiation at bilateral meetings.	Reduction of shipping transit times and costs for Mongolian exports.
A4. Deepening and strengthening of the financial sector	Policy framework and strategy developed to deepen the primary and secondary mortgage markets.	Expanded primary and secondary mortgage markets provide competitive loan products for residential and commercial financing.
	Assessment and plan of action prepared for stock market operations and development of equity products.	Diversity of equity financial products available.
	Implementation of insurance regulatory framework and strengthened sector supervision.	Strengthened regulatory and capacity to supervise a wider range of insurance products.
A5. Response to emerging policy reform initiatives	As negotiated and agreed upon and consistent with project policy support focus on laws, regulations, systems, and procedures directly affecting the business environment.	As defined and agreed upon for each initiative.

For the Energy sector reform support component of the project, the proposed work plan framework is shown below:

B. ENERGY SECTOR REFORM SUPPORT

Policy Support Objectives	Projected annual results	LOP Results
B1. Development and implementation of a transparent, market-oriented regulatory environment to promote competitive and efficient delivery of energy services to consumers	<p>ERA issues regulations and supervises implementation and use of cost-based standards for use by power generating companies .</p> <p>ERA issues and supervises implementation and use of IAS-compliant chart of accounts by power generating companies</p> <p>ERA has strengthened supervisory capacity to oversee power generating companies' implementation of cost-based tariffs and IAS-compliant chart of accounts</p>	The ERA has increased supervisory capacity to regulate a competitive, market-oriented, and transparent regulatory environment in the energy sector.
B2. Development, maintenance, and implementation of commercial orientation and practices in energy generation and distribution companies in the sector	<p>All energy companies are implementing cost-based tariff methodologies and IAS-compliant standard chart of accounts.</p> <p>Some distributions companies are implementing improved customer service practices (complaints management, billing and collection systems).</p>	Energy generation and distribution companies in the sector operate on a commercial basis.
B3. Development, maintenance, and implementation of a legal, regulatory, and financial environment attractive to foreign and domestic private investment and management in the sector	Measures identified and plan of action implemented through "country due diligence" assessment to make Mongolia's energy sector attractive to private foreign investment.	Foreign and domestic private investment transactions negotiated/concluded in the energy sector.
B4. Response to emerging energy sector initiatives	As negotiated and agreed upon and consistent with project energy sector focus on the regulatory environment, commercialization and attraction of private investment and management.	As defined and agreed upon for each initiative.

The corresponding framework for the Business and sector/cluster development component appears as follows:

C. BUSINESS AND SECTOR/CLUSTER DEVELOPMENT

Objectives	Projected annual results	LOP Results
C1. Improved competitiveness of identified sectors/clusters	Foreign target market niches for Mongolian products or services identified in the key sectors of tourism, cashmere, other textiles, meat and meat products, skins, hide, and leather.	Significantly improved access to and penetration of foreign markets through the introduction of best business practice, co-marketing initiatives, and technology/quality up gradation, <i>across the sector</i> .
C2. Improved competitiveness of sector/cluster based firms	Potential 'anchor firms' identified, recruited as clients, and receiving assistance from the Matching Grant Program (MGP). Dialogue initiated between anchor firms and foreign buyers.	Client firms increase sales and market share in export and export oriented markets, <i>i.e.</i> , become more competitive.
C3. Improved competitiveness of <i>high potential</i> client firms regardless of sector	High potential firms identified, recruited, and receiving assistance from the BD program	Improved core business practices (marketing, production, financial and asset management) leads to increased sales, profitability, employment and investment) - the performance indicators.
C4. Response to emerging opportunities to structure and facilitate public or private/public transactions	As negotiated and agreed upon among the parties and consistent with project BD focus on improving competitiveness of firms, sectors/clusters, and country.	Value of transactions structured or brokered.

Cross-cutting activities such as national dialogue and project management constitute the fourth component of the project, as detailed below:

D. CROSS-CUTTING ACTIVITIES: NATIONAL DIALOGUE AND PROJECT MANAGEMENT

Objectives	Projected annual results	LOP Results
D1. Improved public transparency, corporate governance and national dialogue	<p>Not-for-profit organization, the "Mongolian Business Trust" (MBT) registered, operating as a party to BD transactions, providing value-added services to foreign investors and local businesses through the dissemination of information for businesses and con</p> <p>Continued support for the <i>Open Government</i> Web site operated through the MBT.</p> <p><i>The Mongolian Business Trust Quarterly Review</i> is available through a Web site and distributed electronically to subscribers, in English and Mongolian.</p> <p>Public speaking engagements and audience-targeted informal presentation and discussion opportunities by visiting experts, short-term consultants, and project staff are utilized.</p>	<p>A private-sector led, at least partially self-sustaining not-for-profit organization articulates business interests, develops positions on issues, promotes exports and foreign investment in the country, and provides value-added services to its members.</p> <p>Increased national dialogue on economic policy issues and government transparency.</p> <p>Business community, partners and general public are more informed on economic issues, policy options and the functioning of open market economies.</p> <p>World-class technical expertise shared with the general public, partners, and business community.</p>
D2. Coordination and cooperation with partners, foreign investors, bilateral, and multilateral organizations	Regular meetings and discussions lead to identified opportunities to structure collaboration in mutually beneficial ventures.	Increased value-added of project technical assistance delivered through proper project positioning, collaboration, and leveraging of resources.
D3. Monthly EPRC Review	Coverage of project activities of general interest, issued monthly and distributed electronically in English and Mongolian.	Partners are well informed on project activities.
D4. Contract management	Quarterly Progress and Financial reports (QPRs), Annual Work Plans (AWPs), project inventory, training reports, and other contract reports submitted to USAID/Mongolia as required.	Project contractual requirements are met.

C. Work plan implementation

Substantive work was accomplished in all four project components during the quarter under review. Exhibits II-1 through II-4 present AWP-04 implementation details for each.

C1. Economic, trade, and financial policy support

Major activities of this component during the quarter, as described in Section I included the following:

- A comprehensive review of the Mongolian tax system and its impact on competitiveness
- A series of intensive discussions with key GoM counterparts concerning a proposed program of tax reform program to promote job creation, formalization of employment and competitiveness
- Design of interventions to mitigate the potential impact of the end of the Multi Fiber Agreement and the quota system on textiles and apparel exports of Mongolia
- Continued work on the shadow economy survey with the Mongolian Foundation for Open Society (MFOS) and the National Statistical Office (NSO) in preparation for field data collection at the household level.

Additional activities not highlighted in Section I, include the following:

- Assistance provided to the MOIT on TIFA requirements and development of TORs for an international expert to assist the Ministry in preparation for these negotiations.

- Preparation of TORs for an international textile expert to assist MoIT and the apparel industry in the transition from the Multi Fiber Agreement and textile quota system to open markets.

Exhibit II-1, at the end of this section, provides details on overall status of AWP-04 implementation in the Economic, trade, and financial policy support area.

C2. Energy sector reform support

Highlights of energy sector work during the quarter, as detailed in Section I, included:

- Assistance provide to the ERA on construction and electric supply/distribution licenses
- Release of Regulatory Cost Accounting manual and training materials in mini CD
- Completion of training materials for workshops that will begin in early October on account conversion and restatement of accounts in IAFRS format for Central Energy System generating companies
- Continuation of energy sector roundtable discussions, with the fourth session hosted at EPRC
- Preparation and distribution of two policy briefs on national debt and privatization in the energy sector
- Finalization of Terms of Reference (TORs) and contracting for an international expert to assist the ERA on public communication systems and procedures.

By the end of the quarter, Energy Sector Reform activities were proceeding on schedule while responding flexibly to emerging policy issues that needed to be addressed. Exhibit II-2, at the end of this section, provides details on AWP-04 implementation status for this component.

C3. Business and sector/cluster development

Key activities of the Business and sector/cluster development during the quarter, as described in Section I, included:

- Organization of a National Cashmere Conference, in partnership with GTZ, and the first meeting of the group hosted by the project
- Formal constitution of a new Mongolian leather association—Eco-Aris—supported by the project
- Fact-finding tour of tourist facilities, with 38 ger camps visited and the same number of managers interviewed and establishments assessed
- Finalization of share holding arrangements and payment of share capital for the European Distribution Center of Mongolian cashmere products scheduled for opening in Berlin next quarter
- Continued support of the *FiberMark Society*, especially concerning the registration of trademarks in the European Union
- Initiation of the feasibility study for the establishment of a local private equity fund, in partnership with the Mongolian Foundation for Open Society (MFOS)
- Preparation of TORs and engagement of an international textile expert to come to Mongolia in October and assist the GoM by examining textile and apparel cost structures, levels of competitiveness, and proposing potential measures to mitigate the impact of the end of the Multifiber Agreement (MFA)
- Preparation of TORs to assist MoIT in preparation for TIFA negotiations with the U.S.

By the end of the quarter, BDS activities were proceeding as planned although progress was slow in the tourism sector. Although key actors agree with the need for a Tourist Information Center, collaboration is difficult as none wants to relinquish main control of a potential new entity.

Exhibit II-3, at the end of this section, presents details of the AWP-04 implementation of the BDS component.

C4. Cross-cutting activities: national dialogue and project management

As presented in Section I, highlights of the quarter included:

- Release of the mini CD *Essential Business Laws of Mongolia*, in partnership with *The National Legal Center* (NLC)
- Execution of subcontract with *The Asia Foundation* (TAF) to support the *Open Government* Web site and national dialogue activities
- Continued work NLC on revising law-making process to strengthen public participation and dialogue in the process
- Production and distribution of two EPRC Newsletters, one for July-August and another for September, in English and Mongolian

Exhibit II-4, at the end of this section, provides details of AWP-04 implementation status in this area.

D. EPRC-sponsored public conferences, presentations, and training events

Exhibit II-5 summarizes EPRC-sponsored public conferences, presentations, and training events held at the USAID Resource Center during the quarter. A total of 35 participants attended two events sponsored by the project with a total duration of 26 hours for an equivalent of 114 person/days (35 participants x 26 hours divided over 8 hours per day). Training for energy sector companies and regulators on IAFRS-compliant standard charts of accounts and accounting principles accounted for most of the training delivered.

Exhibit II-5: Public conferences, presentations, and events held during the quarter (Jul-Sep-04)

No.	Event code	Date	Event	Target participants	No. of Atten.	Type of event	Duration (Hours)
1	BDS	13 Sept	Roundtable meeting with cashmere manufacturers	Private cashmere companies	12	Round Table meeting	2
2	ENER	28-30 Sept	Training on Regulatory Accounting	Power plants of Erdenet, Darkhan and Ulaanbaatar, CHP, UB Audit	23	Training	24

Totals	35	26
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Event codes: ENER = Energy Support

BDS=Business Development Service

Total person/days:	114
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E. Emerging issues and key actions for the next quarter

Emerging issues and key actions for the next quarter are noted below.

E1. Emerging issues

Negotiations and implementation strategy of proposed tax reforms. While at the end of the quarter there appeared to be broad consensus and sufficient political will to implement the proposed reforms, the bulk of the technical work still lies ahead. The project will continue to exercise its best efforts to act as a neutral technical advisor to the branches of government and diverse political actors and provide all requisite expert resources as needed. Similarly, EPRC will continue to work closely with the International Monetary Fund (IMF), The World Bank, The Asian Development Bank (ADB) and other multilateral and bilateral agencies to insure coordination and complementarity of efforts. An emerging division of combined institutional efforts concerning tax reform would have:

- EPRC concentrate on aligning the current tax regime with overall country competitiveness supportive of private sector-led economic growth
- The prospective IMF mission on taxation focus on aligning tax legislation and regulations with international best practices
- The World Bank and ADB leading a reorientation of budget expenditures towards economic growth support and poverty reduction.

It is likely that, given current time frames for the 2005 national budget approval, the “competitiveness-based” tax measures proposed by the project and those that the IMF mission may suggest could be put together in an amendment after the current budget is approved.

During the next quarter the project will work closely with all parties in the delicate tasks of preserving and enhancing political consensus, assisting with the detailed budget technical analyses, and helping the GoM in the development of a public discussion and communications strategy to support these reforms. EPRC will also coordinate closely with the USAID Mission and the country team whose support for these proposed tax reforms has been exemplary and invaluable.

Assessment of impact of the end of the Multifiber Agreement (MFA) on the Mongolian textile and apparel industry and proposed mitigation measures. During the next quarter an international textile expert will assist local firms, the project, and MoIT in formulating options to mitigate the potential impact of the end of the MFA. Findings of this analysis will be shared and discussed to formulate actionable plans for government and industry implementation. Given the importance of the textile sector in terms of employment and export earnings in the Mongolian economy, the findings, recommendations, and quality of execution of timely actions will prove crucial.

Trade capacity building at the MoIT for under the Trade and Investment Framework Agreement (TIFA) with the U.S. and other bilateral trade negotiations. With the first meeting of TIFA’s Joint Council expected to occur within the next few months, the project prepared TORs for an international expert to improve trade capacity at MoIT. After USAID’s Legal Counsel reviews the TORs, the project expects to field an international trade expert to assist MoIT during the next quarter.

Proposed project assistance strategy to the MoIT in support of TIFA negotiations is based on acting as a catalyst for wider multilateral and bilateral contributions to much needed trade capacity building to enable Mongolia to implement requisite reforms and negotiate bilateral and regional agreements to improve access to markets for its products. The proposed strategy also calls for the establishment of a specialized international trade negotiating unit supported by small technical analysis and public dialogue units relatively independent of civil service constraints. This effort is likely to require a two-year time framework.

E2. Key actions for the next quarter

Major activities or key actions projected for the next quarter are within the framework of key achievable actions proposed under a 100-day plan for the new coalition government. We present below an overview of these as well as AWP-scheduled activities by project component.

Economic, trade, and financial policy support:

- Continued support for the proposed package of tax reforms, one of the core actions proposed under the 100-day plan and likely to absorb most of the resources of the policy component of the project during the next quarter
- As part of the proposed 100-day plan, continue discussions with government on implementing pro-poor policies in a fiscally responsible way
- Proposed policy measures to mitigate impact of end of the MFA on Mongolia
- Assistance with TIFA in time for first meeting of Joint Council
- Execution of subcontract with the Mongolian Open Society Forum for the conduct of a national household survey on the shadow economy
- Implementation of other scheduled AWP-04 tasks.

Energy sector reform support:

- Likely execution of a subcontract with an American legal firm for drafting a Concession Law and due diligence review of pertinent laws and regulations to reduce private foreign and domestic investors' risks, as proposed in the 100-day plan
- Implementation of workshops on conversion of accounts and restatement of accounts according to IAFRS requirements for Central Energy System generating companies
- ERA enactment of public hearing procedures based on international expert's recommendations
- Implementation of scheduled AWP-04 tasks.

Business development services:

- Finalization of proposed EPRC and USAID Mission procedures protocol for engagements funded through the *Competitiveness Fund* and the *Business Development Fund*
- Execution of a subcontract with an American legal firm for the registration of pending trademarks of the *FiberMark Society* in the EU
- Based on international textile expert's recommendations, support discussion and consensus building on actionable industry and government level proposals to mitigate the impact of the end of the MFA on local textile and apparel industry
- Follow up on recommendations from the feasibility analysis for a local private equity fund
- Subcontracting arrangements with The World Economic Forum (WEF) to rank Mongolia in the 2005 Microeconomic Index of Competitiveness

- Work with the Ministry towards the establishment of a private sector-led working group to be assisted by an international expert to be supplied by the project to draft a new Tourism Law
- Prepare promotional and marketing materials and recruit potential clients for the *Competitiveness Fund* and the *Business Development Fund*
- Implementation of scheduled AWP-04 tasks.

Cross-cutting issues: National dialogue and project management:

- Continued work with *National Legal Center* (NLC) and *The Asia Foundation* (TAF) to review process of law submission with the objective of improving citizens' involvement, transparency and usefulness of the *Open Government* Web site—a component of the proposed 100-day plan
- Assist the Mission with its portfolio review and performance indicators relevant to the project
- Review project results for the year and prepare annual work plan for 2005
- Support for the local chapter and potential subcontracting with Transparency International to have Mongolia ranked in their 2005 Corruption Perception Index (CPI)
- Continued upgrading and media promotion of the *Open Government* Web site
- Test and bring on line a project Web site
- Implementation of scheduled AWP-04 tasks.

Exhibit II-1: Economic, trade, and financial policy support work plan implementation (Jul-Sep-04)

A. ECONOMIC, TRADE, AND FINANCIAL POLICY SUPPORT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
A1. Development, maintenance, and implementation of sound macroeconomic policies to promote sustainable and equitable economic growth A1.1 Comparative assessment and benchmarking of corporate and VAT tax policies and administration, formulation of options and action plan		>> >>	>> >X >>	>> >> >>	Completed reform proposal focused on reducing distortion effects of tax provisions on business, submitted proposal to GoM for inclusion in a 100-day reform program. Initial agreement on objectives of tax reform secured from Executive and Parliament. Continued technical work on tax reform package expected to continue through the next quarter.
A1.2 Comparative assessment and benchmarking of income taxation, social contributions, pension policies and administration, formulation of options and action plan A1.2.1 Labor market and payroll fiscal charges: comparative analysis and proposal for reform Policy Brief: Fulfilling campaign commitments in a fiscally responsible way A1.3 Comparative assessment and benchmarking of central budget expenditures, formulation of options and action plan		>> >> >>	>X >> >> >X >> >> >> >>		<p>Proposal complete and submitted. Technical work carried jointly with MoFE and the General Department of Taxation expected to continue through the next quarter.</p> <p>Policy Brief prepared in late September and distributed at Cabinet, Chairs of Parliament Standing Committee, and policy advisors weekend retreat held on 9 October at Ikh Tinger.</p> <p>Concurrent analyses in connection with A1.1 and A1.2.1 activities, as noted above.</p>
A1.4 Foreign debt service assessment, projections and policy options					
A1.5 Real exchange rate management					
A2. Development, maintenance, and implementation of trade and investment policies supportive of a competitive participation of Mongolia in the world economy					

Exhibit II-1: Economic, trade, and financial policy support work plan implementation (Jul-Sep-04)

A. ECONOMIC, TRADE, AND FINANCIAL POLICY SUPPORT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
A2.1 Assessment of tariff and non-tariff barriers to trade in Russia and China.					
A2.2 Utilization of Generalized System of Preferences (GSP) for Mongolian products	>> >>	>> >> >>			Completed data compilation of Generalized System of Preferences (GSP) granted in the U.S.A., Japan, and the European Union as target export markets for potential Mongolian products. Release of user-friendly CD and Web-accessible database with search capabilities delayed.
A2.3 ATC and MFA impact analysis, scenarios, and policy and industry options		>> >> X			Completed draft technical paper prepared on Impact scenarios of the Agreement on Textiles and Clothing (ATC) and Multi Fiber Agreement (MFA) on Mongolian textiles quota-free access to U.S. markets and formulation of policy and industry options.
A2.4 Assessment of advantages and disadvantages of potential FTAs with Russia and China					Formulation of trade policy options re potential FTAs with neighboring countries.
A2.5 Trade policy and trade negotiations					
A2.5.1 Reduction of tariff and non-tariff barriers for Mongolian products with a BD-identified niche demand in specific target markets	>>	X >> >>			Advice submitted to MOIT on tariff reduction application to be made to European Commission. MOIT made application on 25 March 2004. Negotiations have commenced.
A2.5.2 Trade management capacity	>> >> >>	X >> >>	>> >> >>	>> >> >>	Assistance to MoIT provided on an as needed basis.
A2.5.3 Feasibility analysis of Free Economic Zones (FEZ) in Mongolia	>> >X				Completed assessment of Mongolia's Free Trade Zones Program and site evaluations of proposed Zamyn-Uud and Altanbulag FTZ sites.
Policy Brief on Free Trade Zones		>X			Policy Brief on Free Trade Zones prepared and delivered.
A2.5.4 Assistance on FTAs (U.S. and other) and RTAs		>> >X >>	>> >> >>	>> >> >>	TIFA comments submitted to US Embassy. On going preparation of petitions to USTR to expand product coverage under the US GSP 2004 with MoIT submitted in May 2004.

Exhibit II-1: Economic, trade, and financial policy support work plan implementation (Jul-Sep-04)

A. ECONOMIC, TRADE, AND FINANCIAL POLICY SUPPORT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
A3. Reduction of transaction costs for businesses					
A3.1 Review of nominal and real interest rates, Bank of Mongolia policies, banking spreads, and formulation of policy options					
A3.2 Transit of goods through Russia and China				>> >X	Field investigation of Russian and Chinese practices applied to the transit of selected Mongolian products and elaboration of GATT-supported procedures for negotiation at bilateral meetings. Activity will be reprogrammed for AWP-2005 due to focus on assisting MoIT with preparations for TIFA negotiations with the U.S.
A4. Deepening and strengthening of the financial sector					
A4.1 Insurance sector regulatory environment					Activity has been on hold. Likely to be dropped as a result of on going discussions with the Asian Development Bank (ADB). Under third financial sector loan agreement, ADB will take the lead in assisting GoM with regulation in the insurance and non-banking financial institutions; EPRC will focus its assistance on assisting insurance firms in product development and regulatory compliance.
A5. Response to emerging policy initiatives					
A5.1 Countries' best practices, development of economic & financial models to inform the negotiation of stability agreements in the mining sector		>> >X			As negotiated and agreed upon and consistent with project policy support focus on laws, regulations, systems, and procedures directly affecting the business environment.
Policy Brief on Negotiation of stability agreements in mining		>X			Completed assessment of Mongolia's mining sector competitiveness and framework for use of stability agreements at the request of MoFE.
A5.2 Review and updating of Jan-03 draft <i>Economic Development Strategy for Mongolia through 2015</i>	>> >> >X	>>X			Policy brief prepared and delivered.
A5.2.1 Economic Development Strategy Technical Paper: Mongolia's foreign trade		>> >X			Completed third draft of a prioritized development strategy tentatively entitled <i>Mongolia: Vision 2020</i> .
					Technical paper completed in draft form.

Exhibit II-1: Economic, trade, and financial policy support work plan implementation (Jul-Sep-04)

A. ECONOMIC, TRADE, AND FINANCIAL POLICY SUPPORT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
A5.3 Shadow economy survey		>> >> >>	>> >> >>	>> >> >>	Continued working with Mongolian Open Society Forum and National Statistical Office to review data collection instrument and results of field pre-testing of questionnaire. Began subcontract negotiations with OSF to conduct national household survey.
A5.4 Economic policy reform agenda proposal for the new government			>X >> >>	>X	Assistance to the GoM on defining economic policy reform agenda focused on private sector based economic growth and increased country competitiveness. Proposed economic policy reform agenda specified for the first 100 days.
A5.5 Assessment of Mongolia's legal framework for concessions and draft Concessions Law		>> >> X >>	>> >> X		Initial assessment performed at the request of the Ministry of Justice.
A5.6 Mongolia's country risk and country risk premium		>> >> X >> >>	X >> >>	X >> X	Released English version of technical analysis of Mongolia's country risk and country risk premium estimation. Daft translation into Mongolian completed. Meetings held with risk management unit of Mongol Bank, at their request, concerning scheduling of jointly-sponsored workshops on subject matter.

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Updated: 28-Oct-04

Exhibit II-2: Energy work plan implementation (Jul-Sep-04)

B. ENERGY SECTOR REFORM SUPPORT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
B1. Development and implementation of regulatory environment					
B1.1 Regulations and implementation of cost-based standards for sector companies	>> >> >>	>> >> >>	>> >> X		Finalized IAFRS-based Uniform Chart of Accounts for energy sector companies and submitted to MOFE for approval.
B1.1.1 Cost-based tariff calculation by sector companies	>> >> >>	>> >> >>	>> >> >>	>> >> >>	Prepared for second round of workshops to teach IAFRS rules to generating companies and prepared to assist them with account conversion.
B1.1.2 Assist ERA with implementation of an IAS-based Regulatory Accounting System			>> >> >> >>	>> >> >>	Prepared implementation plan for new accounting system to be executed starting on the third quarter of 2004 and continuing through fourth quarter of 2005.
B1.2 Strengthening of ERA supervisory capacity					
B1.2.1 Development and support for ERA system for supervision of and implementation of a reporting system by sector companies.		>> >>	>> >> >>	>> >> >>	Assessed ERA tariff review and audit capabilities.
B1.2.2 Development and support for ERA's public information strategy			>> >>	>> >> >>	Finalized TOR and finished contracting for public hearings short-term specialist to start in early Oct. Assisted with drafting of an interim Public Hearing Procedure.
B1.2.3 Develop Public Hearing Process to hear sector company and Consumer complaints				>> >> >>	Same as above.
B1.2.4 Assist ERA with review of temporary sector company operating licenses and develop long term licenses			X X	>> >> >>	Assisted ERA in drafting standard model for all licenses and assisted with drafting two company specific distribution and supply licenses.
B2. Development and Implementation of commercial orientation and practices in private sector companies					
B2.1 Billing and collection systems for distribution companies					Finalized cost accounting manuals and CDs for sector companies.

Exhibit II-2: Energy work plan implementation (Jul-Sep-04)

B. ENERGY SECTOR REFORM SUPPORT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
B3. Attractive environment for private investment in the sector	>> >>	>> >> >>	>> >> >>	>> >> >>	Initial review of legal conditions for an Infrastructure Concession Law to reduce investors' risk conducted with assistance from short-term specialist. Entered into negotiations with a law firm to draft Concession Law. Prepared two Policy Briefs on Energy Sector Debt and Privatization Plan.
B4. Response to emerging policy initiatives					
B4.1 Assistance to GoM in drafting energy sector legislation and amendments	>> >> >>	>> >> >>	>> >> >>	>> >> >>	Assisted PSC with input for new government privatization plan. Created database of potential hydro electric sites. Advised private developer on coal property development. Assisted private company at USAID request in dealing with MOI on power supply to their mining project.
B4.2 On-demand assistance to ERA	>> >> >>	>> >> >>	>> >> >>	>> >> >>	Supported World Bank projects on tariff design and market structure.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C.1 Improved competitiveness of sectors/clusters					
C 1. 1 Natural fibers (cashmere)					
C1.1.1 Status assessment, strategy, and action plan					
Review of available assessments and reports; site visits to firms, associations, and clusters; identification of supply chains, export capacities, and constraints; identification of anchor firms	>> >> >>				Completed.
Concise sector/cluster status report and proposed strategy elaborated	>>	X			Completed.
C1.1.2 Support to sector/cluster associations					
Assistance to the FiberMark society					
Point of sale (POS) marketing materials for Mongolian cashmere developed and distributed		>> >X	>> >X>>>		Completed.
Market Intelligence Unit established to disseminate information about target export market niches for cashmere			>> >>	>> >X >>	FiberMark society gathering information and disseminating it through weekly newsletter.
Proposal prepared for membership of IWTO				>> >X	
Application prepared for the protection of geographical indication of Mongolian cashmere			>> >> >X		On going.
Cashmere Forum for cluster members conducted		>> X			Cashmere forum held on 6 July. Decision made to form a national cashmere working group.
<i>National Cashmere Working Group established</i>			>	> X	On-going.
Proposal prepared for the accreditation of Textile Institute Laboratory		>> >>	>> >>	X	Delayed due to Textile Institute; re-scheduled for November 2004.
Facilitate the preparation of a Spring Fashion Show 2005			>	>> >>	Preparations commenced.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C1.1.3 Improved marketing and distribution channels in target export niche markets Mongolia' page in Wool Record: Monthly articles on cashmere and wool industry developments Berlin Distribution Center for Mongolian cashmere: Identification and negotiation with partners, business plan developed, company formed and distribution center opened.			>	> > >	Articles written for inclusion in October and November issues Company, 'UB Concept' formed and registered in Germany. Shareholding established and shares paid up. Premises secured. Opening planned for last week in November 2004.
C1.1.4 Improved country competitive environment for the sector Mongolian baseline cashmere competitive value chain analysis completed: volumes, values, capacities, technologies, linkages, major players, profitability, taxation, regulatory, and policy issues at each stage Promulgation of findings and working cluster consensus on taxation, regulatory, and policy priority proposals for GoM consideration Implementation follow-up of taxation, regulatory and policy proposals; briefings to Executive and Parliament members and lobbying			> >>	>X >X >X >>	Delayed due to transfer of effort to MFA issues, planned to start late November.
C1.1.5 Improved business practices and technical knowledge of cluster/sector counterparts Internships Program: Products or deliverables-based projects jointly designed with counterpart agency and implemented with counterparts' personnel seconded temporarily to EPRC Internship 1: Internship 2: Workshops, conferences and training: To disseminate knowledge of best practices, improve technical and management skills Mongol Amicale, Customer Service training completed	X			> > > > > > X> X>	Completed.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C1.1.6. Response to emerging opportunities for firm level transactions					
Mongol Amicale, broking transactions with a Swiss distributor		>> >>			Negotiations failed due to inability of Mongolian processors to meet technical specifications
Ermel, design of a new collection, website, visitor center (potential for BDF)		>> >X			Waiting for commitment to 50% cost share
Altai cashmere, product development		>> >>			Completed.
C1. 2 Tourism					
C1.2.1 Status assessment, strategy and action plan					
Review of available assessments and reports; site visits to firms, associations, and clusters; identification of supply chains, export capacities, and constraints; identification of anchor firms	>> >> >>				Completed.
Concise sector/cluster status report and proposed strategy elaborated	>> X				Completed.
C1.2.2 Support to sector/cluster associations					
Assistance to the Mongolian Tourism Association					
- Insurance workshops		W W	W	W	Two workshops completed last quarter conjunction with Mongol Daatgal and MTA
-Trade show preparation workshops				W	
Dissemination of market intelligence	>> >> >>	>> >> >>	>> >> >>	>> >> >>	Continuous.
Assistance to MTA provided for the preparation of its 2005 business plan				>> >X	
Joint assessment of the current certification system			>X		Field trip undertaken with MTA and MTB. Surveyed 38 ger camps and over 100 international tourists. Recommendations now being collated for submission to new Ministry.
Trade show manual published			X		Manual prepared, will be published November.
Tourism inventory for Zavkhan aimag produced			>>	X	Cancelled due to lack of capacity.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C1.2.3 Improved marketing and distribution channels in target export niche markets Tourist Information Center (TIC): Identification and negotiation with partners, concept and business plan developed and distributed to the tourism cluster, Memorandum of Understanding signed among partners, premises secured, NGO established and co-operation agreement signed, TIC opened	>> >> >>	X >X >>	>> X >>	>X	Concept and business plan for TIC developed, discussed and accepted by cluster. Further progress suspended due to changes within GoM and UB Municipality. Premises withdrawn by UB municipality's new administration
C1.2.4 Improved country competitive environment for the sector Tourism Law: Draft amendments submitted to Mol Tourism sector data improvement: Assessment, design, action plan, and resource requirements proposal prepared and submitted			>> >> X >> >> X		Delayed due to changes in GoM tourism structure (reorganized ministry).
C1.2.5 Improved business practices and technical knowledge of cluster/sector counterparts Internships Program: Products or deliverables-based projects jointly designed with counterpart agency and implemented with counterparts' personnel seconded temporarily to EPRC Internship 1: Internship 2: Workshops, conferences and training: To disseminate knowledge of best practices, improve technical and management skills				> > > X X	
C1.2.6. Response to emerging opportunities for firm level transactions Development of Safari Park concept for Ulaanbaatar (potential for BDF)		>>>>	>> X		STTA completed under BDF. Report and recommendations forwarded to client. Further action under review.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C1.3 Meat C1.3.1. Status assessment, strategy, and action plan Review of available assessments and reports; site visits to firms, associations, and clusters; identification of supply chains, export capacities, and constraints; identification of anchor firms Concise sector/cluster status report and proposed strategy elaborated		>> >>	>> >>		
C1.3.2 Support to sector/cluster associations Assistance to the Meat Producers Association Market Intelligence Unit established Analysis of barriers to export of meat and meat products to emerging markets and presented to the industry STTA to improve sanitary conditions in selected meat processing plants engaged C1.3.3 Improved marketing and distribution channels in target export niche markets Provide market information to meat processors in support of potential exports to Egypt and the Middle East C1.3.4 Improved country competitive environment for the sector			>> >X	X X X	

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C1.2.5 Improved business practices and technical knowledge of cluster/sector counterparts Internships Program: Products or deliverables-based projects jointly designed with counterpart agency and implemented with counterparts' personnel seconded temporarily to EPRC Internship 1: Internship 2: Workshops, conferences and training: To disseminate knowledge of best practices, improve technical and management skills					
C1.3.6. Response to emerging opportunities for firm level transactions					
C1.4 Leather C1.4.1 Status assessment, strategy, and action plan Review of available assessments and reports; site visits to firms, associations, and clusters; identification of supply chains, export capacities, and constraints; identification of anchor firms Concise sector/cluster status report and proposed strategy elaborated		>> >>	>> >>		Completed
C1.4.2 Support to sector/cluster associations Creation of and assistance to the Mongolian Leather Companies Association Association of Mongolian Leather Companies formed Cooperation agreements concluded		>> >> >> X	>> X		Completed. Completed.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C1.4.3 Improved marketing and distribution channels in target export niche markets Investigation into opportunities afforded through import of hides from Russia and re-export to Russian footwear industry			>	> >	Desk top research completed, feasibility established. Delegation to visit Russia planned October/November
C1.4.4 Improved country competitive environment for the sector					
C1.2.5 Improved business practices and technical knowledge of cluster/sector counterparts Internships Program: Products or deliverables-based projects jointly designed with counterpart agency and implemented with counterparts' personnel seconded temporarily to EPRC Internship 1: Internship 2: Workshops, conferences and training: To disseminate knowledge of best practices, improve technical and management skills					
C1.4.6 Response to emerging opportunities for firm level transactions					
C2. Sector/cluster transaction support: The Mongolian Competitiveness Fund C2.1. Assessment and fund design Fund design requirements document completed based on local assessments; proposed objectives, operations, client eligibility, management and monitoring mechanisms agreed upon.	>>	X >>	X		Completed.
C2.2. Fund marketing and promotion Marketing brochures, media materials and roll-out plan prepared Marketing workshops, seminars and press conferences delivered			>>X W W		Delayed due to longer than expected review procedures. Planned for final quarter.

Exhibit II-3: Business development services work plan implementation (Jul-Sep-04)

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

AWP-2004 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
C2.3. Client recruitment and transaction structuring Clients assisted in project formulation, subcontracts negotiated, and projects monitored			>> >>	>> >> >>	First transaction under way.
C2.4. Quarterly report on fund management results Quarterly report on transaction pipeline and transaction results			>>	X	
C3. Firm-level transaction support: The Mongolian Business Development Fund C3.1. Assessment and fund design Fund design requirements document completed based on local assessments; proposed objectives, operations, client eligibility, management and monitoring mechanisms agreed upon.		>> >> X			Completed.
C3.2. Fund marketing and promotion Marketing brochures, media materials and roll-out plan prepared Marketing workshops, seminars and press conferences delivered			>X >> W	W	Delayed due to longer than expected review procedures. Planned for final quarter.
C3.3. Client recruitment and transaction structuring Clients assisted in project formulation, subcontracts negotiated, and projects monitored			>>	>> >> >>	First transaction under way.
C3.4. Quarterly report on fund management results Quarterly report on transaction pipeline and transaction results					
C4. Improved competitiveness of business environment C4.1 Inclusion of Mongolia in 2005 Microeconomic Index of Competitiveness				>> >> X	Negotiations began with the World Economic Forum to rank Mongolia on the 2005 Index.
C4.2 Feasibility analysis for local private equity fund			>> >>	>>X	Feasibility study began in partnership with <i>The Open Society Forum</i> . Initial findings scheduled for presentation by mid October.

C. BUSINESS AND SECTOR / CLUSTER DEVELOPMENT

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Exhibit II-4: Cross-cutting issues: National dialogue and project management work plan implementation (Jul-Sep-04)

D. CROSS-CUTTING ISSUES; NATIONAL DIALOGUE AND PROJECT MANAGEMENT

AWP-2002 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS	
	Quarter 1	Quarter 2	Quarter 3	Quarter 4		
D1. Improved public transparency, corporate governance and national dialogue						
D1.1 Mongolia Business Trust					On hold until Business Development Fund generates pipeline of transactions, with creation dependent on types of transactions identified.	
D1.2 Open Government Website					Subcontract signed with <i>The Asia Foundation</i> (TAF) for <i>Open Government</i> Website and national dialogue support. Work started with National Legal Center on standard operating procedures for updating, maintaining current, and posting on the Web Mongolian versions of all laws; OG Website would provide links to the prospective NLC Website.	
D1.2.1 Review of relevant laws and resolutions on law-making processes		>> >>	>> >>	X	Completed translations of GoM Resolution 2000-No 178 on Cabinet Procedural Rules, Law on Drafting and Submitting Laws & Other Resolutions of the Ikh Hural of 8 November 2001; Resolution of Ikh Hural of 21 June 2001, No. 61 and its Amendment of 13 May 2004 establishing legal process of law making. Legally-mandated flow will be examined against current practice to generate proposal for reviewing flow to strengthen public participation and transparency in the process.	
D1.2.2 Proposal to Cabinet and Ikh Hural for improved public participation in law-making process and role of Open Government Website		>>	>> >> >>	>> >>	X	Subcontractor TAF, working with <i>The National Legal Center</i> (NLC), began taking the lead on analyzing and flow-charting current law-making process with objective of improving public dialogue and participation.
D1.2.3 Operations and maintenance of the Open Government Website	>> >> >>	>> >> >>	>> X >>	>> >> >>		<i>Open Government</i> Web site is undergoing changes to improve quality of content and access to documents. Project is preparing to provide in-house technical support for Ministers' on-line "chats", beginning next quarter. Site now supports access to transcripts of prior chats.
D1.3 Proposed EPRC Project Web site (in lieu of The Mongolian Business Trust Quarterly)			>> >X			Dissemination of technical reports will be better accomplished through a project Web site in lieu of the initially proposed <i>Mongolian Business Trust Quarterly</i> . Design of the project Web site completed during the quarter. Testing and rollout of the Web site is scheduled for the Oct-Dec quarter.

Exhibit II-4: Cross-cutting issues: National dialogue and project management work plan implementation (Jul-Sep-04)

D. CROSS-CUTTING ISSUES; NATIONAL DIALOGUE AND PROJECT MANAGEMENT

AWP-2002 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
D1.4 Speakers Program	X X	X	>> X		National Cashmere Conference, jointly sponsored by the project and Deutsche Gesellschaft fuer Technische Zusammenarbeit (GTZ), was held at the Chinggis Khan Hotel, Ulaanbaatar, on 6 July 2004. Project-supported new Mongolian leather processors association, ECO-ARIS, held press conference on 7 July 2004.
D1.5 Assistance to the GoM with the <i>Millennium Challenge Account</i>		>> >>			At the request of the Prime Minister's Office, project provided support on MCA indicators, eligibility requirements, and likely project selection criteria to the MCA Inter-Ministerial Working Group created by Cabinet resolution. Project involvement in MCA activities was stopped, following instructions for non-involvement by U.S. Government funded projects.
D2. Coordination and cooperation with partners, foreign investors, bilateral, and multilateral organizations					
D2.1 Energy Donor Round Tables	X	X	X	X	Fourth Energy Donor Round Table was held at EPRC on 27 August. Subjects of major discussion were energy conservation, updating the energy law, technical assistance to the National Distribution Center and privatization efforts in Zavkhan Aimag.
D2.2. USAID Business Development Projects Meetings		X X	X X X	X X X	Monthly meetings held.
D2.3 Millennium Challenge Corporation	>> >>	>>			Intensive assistance provided to MCA Inter-Ministerial Working Group until USAID/W issued guidance of non-involvement
D3. Monthly EPRC Review	X X X	X X X	X X X	X X X	Two issues of the EPRC Monthly Newsletter produced and distributed in English and Mongolian during the quarter, for a running total of eight for the current AWP. (July and August 2004 was a single issue).
D4. Internship program					
D4.1 On-line access to current business laws and English translations - National Legal Center		>> >>	>> >X>>	>> >> X	Activity started during the quarter, with expected MOU and internship program to begin next quarter.
D5. Contract management					
D.5.1 Quarterly Progress Reports	X	X	X	X	Submitted Quarterly Progress Report for the April - June 2004 quarter.

Exhibit II-4: Cross-cutting issues: National dialogue and project management work plan implementation (Jul-Sep-04)

D. CROSS-CUTTING ISSUES; NATIONAL DIALOGUE AND PROJECT MANAGEMENT

AWP-2002 ACTIVITIES	DELIVERABLES & BENCHMARKS				END OF QUARTER STATUS
	Quarter 1	Quarter 2	Quarter 3	Quarter 4	
D.5.2 Annual Work Plans and budgets		>> >X			Updated LOP budget prepared and submitted. Contract amendment negotiations concluded to redesign the matching grants program into two pass-through funds, the Mongolian Competitiveness Fund to support cluster development and the Business Development Fund to assist businesses.
D.5.3 Training database					
D.5.4 Other reports on demand		X X X	X X X	X X X	Monthly project status reports produced.

File: QPR Jul-Sep-04.xls

Updated: 28-Jul-04

SECTION III: PROJECT MANAGEMENT AND ADMINISTRATION

A. Introduction

This section summarizes significant project management and administration activities, problems encountered and actions taken to solve them, and main activities scheduled for completion during the next quarter. Annex B contains a list of long-term local project staff and short-term expatriate technical assignments. Annex C has a budget status report as of the end of the same period.

B. Significant project management and administration activities

Project management efforts during the quarter focused on:

- Working closely with the Mission and the Contracting Officer to sign a contract amendment to capture expenditures in the energy sector support component of the project under CLIN 004 in lieu of the costs of the internship program previously subsumed under this CLIN, restructure the matching grants program into two product-oriented funds—the Competitiveness Fund and the Business Development Fund—and included support for the USAID Resource Center and the Open Government Web site
- Coordinating strategy and implementation of a package of economic policy and transparency reforms achievable in the first 100 days of the new administration
- Participating in intensive discussions with government counterparts and setting the strategy for a package of proposed tax reforms to promote job creation, formalization of employment and competitiveness
- Project hosting of chat services for the *Open Government* Web site and overseeing the internal development of the project Web site.

By the end of the quarter the relative lull of the prior quarter due to national elections had been replaced by an unprecedented level of project activities.

C. Personnel

Mr Christopher Broxholme, Trade Advisor and Deputy Chief of Party, was medically evacuated from post on 30 August. His departure did not materially affect contract performance and all other key contract personnel continue to implement the scheduled work plan activities. As Mr Broxholme's medical clearance status is not expected to be resolved until next spring, the Contractor will formally propose options to the Mission and Contracting Officer regarding this key personnel position.

C1. Long-term local personnel

One long-term local professional resigned during the quarter to pursue graduate studies abroad. Two local support staff also tendered their resignations during the same period. Project management began recruitment of replacement staff, interviewed, and selected suitable

replacements expected to begin work during the quarter. Exhibit B-1 in Annex B provides a summary status of local staff as of the end of the reporting period.

C2. Deployment of short-term expatriate technical assistance

Fielding of short-term expatriate assignments resumed after being largely put on hold last quarter due to national elections. One short-term expatriate technical assignment was completed and four were underway, for a total of five assignments for the quarter. Exhibit B-2 in Annex B provides details about the purpose of these assignments, dates of arrival and departure.

D. Status of subcontracts

A subcontract with *The Asia Foundation* was finalized during the quarter and redefined their scope of work to focus on the public dialogue activity and support of the *Open Government Web* site.

E. USAID Resource Center utilization

Exhibit III-1 summarizes use of the USAID Resource Center by external organizations during the quarter. Use was equivalent to 1,642 person/days.

Exhibit III-1: External events held at the USAID Resource Center during the quarter (Jul-Sep-04)

No.	Event code	Date	Event	Target participants	No.of Atten.	Type of event	Duration (Hours)
1	HRDC	19-Jul	Role of media on combatting human trafficking	Attorneys	8	Presentation	4
2	HRDC	25-26-Jul	Role of media on combatting human trafficking	Lawyers	10	Presentation	4
3	MT	29-Jul	Introduction of Multimedia University	Press, Media	12	Press Conference	2
4	WV	11-13 Aug	Training for regional branches	Branches of WV	38	Training	24
5	CHF	23-24 Aug	Training and meeting for country representatives	Branches of CHF	50	Training	16
6	MAA	9-Sep	Current situation of Mongolian advertisement	Press, Media	7	Lecture	2
7	TCWRP	14-Sep	Presentation on Japanese Aviation Academy by the President of the Academy	Students of Kharkhorin university	26	Lecture	5
8	GAC	15-Sep	Forum of female film makers	Movie producers, NGO	21	Round Table meeting	4
9	APSW	20-Sep	Inclusion of child labor subject matter in university curricula	University teachers	15	Meeting	2
10	DEC	24-Sep	Politics and Civil Society	NGOs	12	Meeting	3

Totals: 199

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Event
codes: WV=World Vision

CHF=Community Habitat Finance
ENER = Energy Support
MAA=Mongolian Advertisement Agency
BDS = Business Development services
TCWRP=The Citizen Will-Republican Party
APSW=Association of Professional Social
Workers
DEC=Democratic Education
Center
GAC=Glob Art Center
HRDC=Human Rights Development Center
MT=Master Travel

Total	
Person/days:	1,642

F. Budget status report

Annex C shows presents the project budget status showing all amounts invoiced during the quarter, cumulative totals, and funds remaining by budget CLIN. The numbers are rounded to the nearest dollar.

G. Problems encountered and remedial actions

There were no significant problems materially affecting contract performance during the quarter. Preparation for and scheduled government elections created an expected gap in government counterparts with authority for policy dialogue and decision making. As a consequence, delivery of short term technical assistance in the policy area was largely put on hold until new government counterparts assume office. Nevertheless, project management and the Mission worked closely together to resume the pace of activities and by the end of the quarter this pace was at an unusually high level.

H. Project and contract management actions expected for the next quarter

Project and contract management actions expected to be completed during the next quarter include the following:

1. Annual performance review of project results in conjunction with the Mission's portfolio review
2. Elaboration, discussion with Mission and counterparts, and submission of the project annual work plan for 2005
3. Testing and rollout of a project Web site to disseminate technical documents and information about the project
4. Negotiation and signing of a Memorandum of Understanding with the National Legal Center—put on hold last quarter due to the intensity of project activities—to update essential business laws in English and Mongolian and make these publicly accessible through their Web site, with linkages from the *Open Government* Web site

5. Transfer of surplus equipment under contractor's custody, with consent from the GoM and USAID—a task currently on hold until the Prime Minister's office appoints an officer in charge of liaison with the project.

ANNEXES

ANNEX A: SUMMARY PROJECT DESCRIPTION



Economic Policy Reform and Competitiveness Project

Activity duration:

17 September 2003 to
16 September 2008

USAID Contract No.:

438-C-00-03-00021-00



Implemented by:



Chemonics International Inc.

In association with:

The Services Group Inc.
Dexis Consulting Group
The Asia Foundation
Crimson Capital
Making Cents

Key personnel:

Fernando Bertoli, *Chief of Party*
Christopher Broxholme, *Deputy Chief of Party*
Janusz Szyrmer, *Senior Policy Advisor*
Bruce Harris, *Senior Competitiveness Advisor*
Horst Meinecke, *Senior Energy Advisor*

Purpose of the activity

Accelerate and broaden sustainable, private-sector-led economic growth through an improved enabling environment for private sector growth and more competitive industries and sectors.

Project goals

1. Accelerate and deepen the policy reform process in Mongolia
2. Promote increased competitiveness in the Mongolian economy.

Project vision

Support a competitive participation of Mongolia in the world economy.

Project strategy

- Continuation of the development, maintenance, and implementation of sound, market-oriented macroeconomic, trade and investment, sectoral, and microeconomic policies that promote sustainable and equitable economic growth
- An enabling business environment and regulatory framework that fosters competition and attracts foreign investment and best business practices
- The development of private sector businesses and clusters focused on supplying the demand of target export and domestic market niches capable of turning and maintaining comparative advantages into competitive edges
- Continued national dialogue on building a national consensus to "put Mongolia on the world map" supported by government transparency and good governance business practices

Project tasks

- **Policy analysis, formulation and implementation support:** This task category includes: (a) policy assessment and analysis; (b) formulation of policy options for improving the competitiveness of the Mongolian economy; (c) assistance in consensus building; and (d) technical and managerial implementation support.
- **Consensus building, public education and national dialogue:** EPRC supports an improved environment for government transparency and corporate governance by working with national decision-makers, the business community, local government and community leaders, academic institutions, and representatives of civil society using a consensus building strategy linked to policy reform and private sector led economic growth.
- **Cluster development and support:** EPRC works with individual firms and inter-related groups (clusters) in key industrial sectors to develop competitive, export-driven businesses. Priority sectors include cashmere, tourism, hides, skins, leather, meat, and textiles.
- **Energy sector support:** EPRC supports Mongolia's efforts to develop and implement a transparent, market-oriented regulatory environment to promote a competitive and efficient delivery of energy services to consumers; commercial practices in energy generation and distribution; and an environment attractive to foreign and domestic private investment.
- **Internship Program:** To improve the quality of economic, trade, and business decision-making, EPRC runs a small internship program where participants acquire first-hand experience in best practices by working side by side with experts on specific projects focused on improving the competitiveness of the Mongolian economy.

ANNEX B: LONG-TERM LOCAL PERSONNEL AND EXPATRIATE SHORT- TERM ASSIGNMENTS

Exhibit B-1: Local long-term project staff as of the end of July–September 04 quarter

Employee name	Position	Start date	End date
<i>Professional Staff</i>			
Altansukh Tumenjargal	IT specialist	10-Nov-03	22-Sep-04
Amgalan Nordov	Energy specialist	10-Nov-03	
Jigjidmaa Dugeree	Business development advisor	8-Dec-03	
Indraa Bold	Business development advisor	5-Jan-04	
Munkhtulga Khurelbaatar	Translator/Interpreter	18-Mar-04	
Odonmijid Ganbold	Accountant	27-Apr-04	
Ashidmaa Dashnyam	Financial and Business Specialist	10-May-04	
Doljinsuren Jambal	Economic Analyst	17-May-04	
Bolor Purevdorj	Translator/Interpreter	19-May-04	
Munkhsaikhan Dambiinyam	Accounting Specialist	26-May-04	
<i>Support Staff</i>			
Uurtsaikh Sanghi	Operations manager	10-Nov-03	18-Aug-04
Khaliun Yura	Receptionist	26-Nov-03	
Oyuntsetseg Minjin	IT assistant/Information officer	12-Dec-03	
Bulgan Narankhuu	Administrative assistant	23-Jan-04	
Odgerel Myagmar	Business development assistant	26-Jan-04	
Batmunkh Batsuren	Driver/Messenger	1-Feb-04	
Erdenebat Dangaasuren	Driver/Messenger	6-Feb-04	
Mandalmaa Dashdorj	Administrative assistant	22-Mar-04	30-Sep-04
Munkhtuya Ganbaatar	Replacement for Bulgan N.	25-Aug-04	

Exhibit B-2- : Short-term technical assignments during the July–September 04 quarter

Name	Purpose of assignment	Date of arrival	Date of departure
Jeff Meller	Concession law and legal framework	10 Jul	23 Jul
Rup Khadka	Overview of the Mongolian tax system	26 Jul	-
Larry Jensen	Implementation of uniform system of accounts	15 Aug	-
Jeremy Burgess	Feasibility study for open zoo	28 Aug	-
David Snelbecker	Assistance on 100-day program for GOM	24 Sep	-